

MEETING SUMMARY

State/EPA SRF Work Group Meeting

May 6-7, 2003

Washington, DC

- I. Welcome and Introductions** - George Ames, EPA Headquarters and Walt Baker, Utah
(See Attachment 1 for a complete listing of meeting attendees.)
Ground Rules - Ian Kline, Facilitator

II. Report by Work Group Enhancements Subgroup

Sheila Platt explained that six state work group members will need to be replaced by the November meeting in Boston. She invited everyone to provide names of potential replacement candidates to Tim Banks. In addition, each work group member should identify a specific alternate that can attend work group meetings in his or her place. The alternate must be from a state in the same geographic subgroup and from the same program area (i.e., CWSRF, DWSRF, or Finance) as the work group member.

Tim Banks explained that he and Walt Baker had tried something new by soliciting agenda topics from every state. Every state representative was asked to submit issues to be addressed by EPA. Those agenda topic suggestions that were not specifically included in the agenda have been responded to in writing by EPA (See Attachment 2 for responses).

George Ames provided an update on establishing a list serve for the work group (an idea discussed at the last work group meeting). This communication tool would cost more money than EPA originally thought. EPA's budget this fiscal year (FY) is not sufficient to maintain the list serve (estimated annual cost of \$2,000). Alternative suggestions from the work group included using a free public service or an established list serve from an industry group (like CIFA or ASIWPCA). Most work group members thought that the list serve would be useful and should be made available to every state SRF program. Mr. Ames pledged to continue to pursue the list serve but cautioned that it might not be possible until the next FY. He will report on the progress at the November work group meeting. Since the last work group meeting, EPA has established a website where the agenda and minutes of each meeting are posted. The website is <http://www.epa.gov/safewater/dwsrf/srfwg.html>

Walt Baker announced that this is his last meeting as Co-chair. Mr. Banks, the current Vice-chair, will assume the position of Co-chair at the end of the May meeting. The work group voted to elect a new state Vice-chair. About half of the work group was eligible, but most of the members had removed their names from contention. Mr. Baker assured state members that the time commitment has been small—most of the time was spent setting up an email distribution list. The other primary duty was assisting EPA in

creating the agenda. Later in the day, the state work group members unanimously selected Greg Mason, Georgia, to serve as Vice-chair.

III. FY 03/FY 04 Budget Status - Sheila Frace and Chuck Job, EPA Headquarters

The FY 03 budget is tight—EPA has cut extramural funding (administrative support and contracts) by approximately 30%. The outlook for FY 04 is similar. In the face of tight budgets and competing priorities (such as homeland security), the funding of the SRFs will remain strong. The Administration has committed to extending CWSRF funding (at \$850 million per year) through 2011—a \$4.4 billion increase over previous commitments. In addition, the Administration has committed to maintaining DWSRF funding at \$850 million through 2018, which is a 140% increase over the previous commitment.

In addition to these commitments, examinations of the nation's approach to infrastructure investments in hopes of identifying how to increase economic and environmental efficiencies are occurring at the same time. EPA is determining how to promote and facilitate water efficiency, asset management, pricing, and fiscal sustainability. Assistant Administrator (AA) Tracy Mehan has emphasized sustainable infrastructure and a watershed approach to managing the nation's water resources. States will be the key to innovation.

Chuck Job added that it is important to recognize the new commitment to the DWSRF—funding will continue for the next fifteen years. In the face of tight budgets, EPA has had to cut the budget of efforts like the Drinking Water Needs Survey. As a result, EPA is not going to be providing the same level of assistance to states that was available for the previous Needs Survey.

IV. Updates

Infrastructure Forum - Chuck Job, EPA Headquarters

On January 31st, Administrator Christine Todd Whitman kicked off the water infrastructure forum, and AA Mehan followed with a keynote address emphasizing non-structural solutions such as asset management, water efficiency, full-cost pricing, water quality trading, public education, and watershed management. Over 270 people attended the forum. The discussion focused on finding alternative ways to increase funding and improve the management of our investment. A constant theme was education—EPA can play an important role by informing the public about the true costs of providing water services and facilitating information sharing within the industry. A summary of the proceedings is available on the Office of Water website. EPA is in the process of identifying follow-up steps to the forum.

E.O. on Project Labor Agreements - Sheila Platt, EPA Headquarters

The Executive Order (E.O.) on Project Labor Agreements (PLAs), issued February 17, 2001 is a federal cross-cutting requirement that applies to all SRF projects. Under E.O.

13208, recipients of SRF assistance may neither require nor prohibit a contractor or subcontractor from entering into a PLA. States should have been implementing this E.O. since October 18, 2002, but do not need to apply the E.O. retroactively. EPA will be including a grant condition as a reminder to states on the requirement in future capitalization grants.

CIFA's Self-certification Proposal - Sheila Platt, EPA Headquarters

On May 9, 2003, CIFA representatives will meet with Jim Hanlon and Cynthia Dougherty to discuss CIFA's proposal for CWSRF self-certification. EPA will report back to the work group on any developments that may result from this meeting.

Status of Off-stream Reservoirs - Kimberley Roy, EPA Headquarters

Some systems employ off-stream reservoirs as a form of pre-treatment to prevent treatment facilities from being overwhelmed during periods of high turbidity. The DWSRF regulations only allow funding for reservoirs in two cases: if they are finished water reservoirs or if they are part of the treatment process and are on the property where the treatment facility is located. However, there may be cases where it is physically infeasible to place the reservoir on the property of the treatment plant. Some states have asked EPA to reconsider its policy for off-site reservoirs that provide pretreatment, not merely storage.

EPA is considering a policy and/or regulatory change to allow off-site reservoirs that comply with a specified set of criteria. The proposed criteria would include size restrictions and a limitation on partial funding (to prevent systems from adding extra capacity for storage). As part of an action item from the last work group meeting, the draft criteria were shared with Mr. Banks and Mr. Jay Rutherford for their review. They were generally supportive of the proposed criteria.

Although EPA has not yet determined how to proceed, it may try to make a change to the DWSRF regulation as part of the Long Term 2 Enhanced Surface Water Treatment Rule development process. EPA recently issued a deviation from the regulations to allow Ohio to fund an off-stream reservoir that met the criteria in the proposal. EPA's intent is to handle such projects on a case-by-case basis until the policy is formally changed.

Investigations of SRFs - Sheila Platt, EPA Headquarters

EPA's Inspector General (IG) in conjunction with EPA has formed a risk identification work group to investigate areas of risk in the SRF programs, such as repayment and disbursement, and the controls in place to minimize these risks, such as audits. The intent is to help the IG improve its audit process by focusing on the highest risk areas. The work group will submit a report of its findings to EPA and OIG management in June 2003. Management will then determine what risks, if any, need to be addressed. EPA will report to the work group on the findings at the November meeting.

Status of CW/DW Needs Survey - Sheila Platt and Kimberley Roy, EPA Headquarters
OMB is currently reviewing the 2000 Clean Water Needs Survey. EPA anticipates sending the final survey report to Congress in July or August 2003. Several factors, including a staffing shortage and the added complexity of documenting NPS needs, have slowed the finalization of the Clean Water Needs Survey. Each step in the study took longer than predicted.

The 2003 Drinking Water Needs Survey is in the data collection phase. The capital investment needs are being collected using a state-specific sample of medium systems serving between 3,300 and 40,000 people and a census of large systems serving over 40,000. Because of major budget reductions, states have the sole responsibility for collecting data, which differs from the last survey when EPA assisted states with improving response rates and helping systems complete the questionnaire. The results of the questionnaires are posted on the needs survey website, where states can review the data and submit modifications. As of the end of April, EPA had received 14% of the questionnaires from the states, which is well behind schedule. The end of the data collection period is November 2003.

Discussion

Several states are having difficulty getting water systems to respond to the DWSRF Needs Survey data request. Some states expressed concerns about the possibility in the future of basing allotment of CWSRF funds on the needs surveys because that would create incentives for states not to address their needs in order to maximize federal funding. These states urged EPA to consider other factors, such as state population and state water quality efforts. Other states expressed concern that the clean water needs estimate is incomplete because it excludes private systems and does not adequately capture nonpoint source (NPS) needs. EPA reminded state work group members that the needs surveys are important data sources for efforts such as the infrastructure gap analysis.

Handbook on Coordinated Funding - Kimberley Roy, EPA Headquarters
A draft of the handbook on coordinated funding has been developed. The handbook discusses the factors a state could consider when establishing a coordinated funding program. The handbook presents the approaches of six states – Arizona, California, Montana, New York, Pennsylvania, and Washington – that have successfully coordinated drinking water and wastewater infrastructure funding programs. It also includes a matrix of the coordinated funding efforts for all states. The draft is currently being reviewed by Steve Grossman's Small Community Water Infrastructure Exchange and the six states that were surveyed. EPA hopes to have a final publication by the end of June.

Status of EFAB Papers - Tim McProuty, EPA Headquarters
The Environmental Finance Advisory Board (EFAB) was chartered in 1989 and has 27

members representing the financing industry as well as state and local government. EFAB was created to provide advice to EPA administrators on how to pay for environmental protection. The board has been undergoing reorganization. The public finance work group, chaired by Sonia Toledo of Lehman Brothers, is currently focusing on funding water infrastructure. EFAB is finishing a report examining ways to improve coordination between SRF and RUS. The paper should be released in the next couple of months. In addition, the public finance work group is looking into the issues of GASB 34, affordability criteria, water conservation programs, watershed and NPS pollution issues, environmental management systems, and joint operations between the DWSRF and CWSRF.

Recent Publications - Kimberley Roy, EPA Headquarters

EPA released a fact sheet on using the DWSRF for transmission and distribution needs. It is available on EPA's website at <http://www.epa.gov/safewater/dwsrf.html>

V. Performance Measures for SRFs

The work group formed a subgroup on environmental/benefit indicators at the last work group meeting. The subgroup started by looking at a suite of environmental indicators created by a previous subgroup. The subgroup held several conference calls to discuss these indicators.

There are a number of program activity measures (PAMs) being proposed for the SRF program as part of EPA's strategic plan. The PAMs are either targets with specific goals in place to be reached by 2008 or indicators. EPA's OWM is currently developing its response to the OMB Program Assessment Rating Tool (PART) budget exercise. The PART has four components: program purpose/objective; strategic planning; program management; and program results. EPA's input on the PART evaluation of the CWSRF program is due to OMB in late May 2003. To measure favorably, a program needs to have strong linkages between its strategic goals and program results. There is limited data to determine the environmental effectiveness of the CWSRF program at this time. EPA needs to identify ways to measure environmental results from the CWSRF. In addition to measuring environmental benefits, EPA and states should determine a way to measure economic benefits.

Georgia's new governor is trying to define "kitchen table" indicators. The state has worked with CIFA to poll twenty states on how they measure benefits. The state identified four categories of benefits (see Attachment 3). The state is planning on releasing a report on these indicators in August 2003.

EPA is currently doing some background research on possible methods for better estimating environmental and economic benefits of the SRF programs. Much has been done on estimating financial benefit, but little has been done on measuring environmental benefit. EPA is considering modeling for both environmental and economic benefits. On the CWSRF side, there have been efforts to document the amount of pollutants that have

been removed, but there has been little effort to link these benefits to federal and state investments. EPA is looking at available data to tie environmental improvement to SRF investment. Some possibilities might be to examine benefits at a municipal, watershed, or national level (rather than at a utility level).

Discussion

EPA asked states whether they had data to help EPA connect DWSRF assistance to the strategic goal of ensuring that 95% of the nation's population is served by a community water system in compliance with the Safe Drinking Water Act (SDWA). Some states create a list of the DWSRF projects that resolve MCL violations every year. Washington is trying to create performance measures by transferring the responsibility to systems as a condition for receiving assistance. Oklahoma is trying to identify problem correction upfront in the application process and then make that information part of their annual report. States suggested that the state annual/biennial reports are probably the best source of information because they should identify why each project was funded. However, the level of detail varies by state.

VI. Legislative Activities on the Hill - Susan Bodine, Chief Counsel of the House Water Resources and Environment Subcommittee

The proposed HR 1560 would reauthorize the CWSRF; there is not yet a house DWSRF reauthorization bill or a Senate CWSRF/DWSRF bill. Because jurisdiction for the DWSRF and the CWSRF is split between two House committees, reauthorization for the SRFs would have to be accomplished with two separate bills. HR 1560 is similar to last year's reauthorization bill. The most contentious issue in the current bill is the Davis-Bacon issue.

Recent studies have shown that the infrastructure need depends on the efficiency of systems. Therefore, HR 1560 creates incentives to generate these cost-saving efficiencies. Congress intends to close the gap largely through increases in efficiency. Congress is concerned that systems do not know the condition of their distribution infrastructure. Therefore, HR 1560 contains a provision for asset management of new infrastructure.

In addition, HR 1560 proposes a CWSRF funding level of \$20 billion over five years. There are provisions for additional subsidies for disadvantaged communities and pockets of low-income communities within cities and towns. The biggest hurdle for reauthorization is the disagreement over Davis-Bacon, especially in the Senate.

Discussion

Some work group members were concerned that the proposed legislation still included some grants. These members would prefer to see all money funneled through the

CWSRF and to allow states the flexibility to provide subsidies, such as negative interest rate loans. Members also expressed concerns that State and Tribal Assistance Grants (STAG earmarks) create disincentives for asset management and should be discontinued by Congress. Some members argued that asset management provisions will negatively impact public health because states do not have the staff or budgets to comply with additional regulatory provisions. State members are concerned that utilities forced to the private market may not be able to find financing and may miss out on the value-added aspects of the CWSRF program. Additional strings make it harder for states to help small systems, which are the systems that need the most help.

Susan Bodine stated that the changes proposed in the reauthorization bill are intended to enhance the impact of limited Federal assistance. Congress does not believe it is increasing the burden on states since many states and well-run systems are already implementing asset management. The provisions in the proposed bill are not full asset management, but only asset management for a project that is receiving public assistance. The reauthorization bill also does not establish capacity development provisions, such as those on the drinking water side. The proposed bill also contains hold-harmless provisions so that no state will experience a decrease in funding in the allotment formula. To make the case for more funding, states need to be able to quantify the benefits of their programs.

VII. Coordination on STAG Earmark Projects - Walt Baker, Utah and Larry McGee, EPA Headquarters

Walt Baker surveyed each state on STAG earmark projects. He asked them four questions:

- Are you delegated to administer STAG grants?
- Do you coordinate with grantees/EPA?
- Do you communicate with Congress?
- Who takes the lead on NEPA?

Based on state responses, 23 states accept STAG administrative funds from EPA, and 4 states are in the process of applying. Most states have no communication with Congress. Sixteen states take the lead on NEPA reviews, six states share the lead on NEPA, and 23 states allow EPA to take the lead.

Larry McGee, EPA's national program manager for STAG earmarks, explained that the number of STAG grants has been increasing steadily since 1997, when there were only eighteen earmarks. In 2002, Congress approved 337 earmarks, and that number is expected to approach 494 this year. Because of the late appropriation this year, few grants from the FY 03 appropriation are likely to be awarded this year. This will add to the already large backlog of earmark grants. At EPA's current pace of processing 180 grants per year, the backlog is approximately three years. Congress is earmarking money for more and more projects for smaller and smaller amounts. These small grants are actually more difficult for EPA to administer because they are going to smaller and

smaller communities, which need more assistance.

STAG grants are unusual in that they are authorized by the appropriation and are not subject to either the Clean Water Act (CWA) or the SDWA. STAG grant projects must meet all other federal cross-cutter requirements and must receive a 45% match (which can come from SRF funds). In 2000, EPA established a 3% set-aside that could go to state agencies, the Army Corps of Engineers, or a national contractor to administer STAG grants.

EPA has agreed to help administer these earmarks to ensure that they follow all applicable rules, but that administration should not be interpreted as support. There is no deadline for STAG earmarks—EPA can ask Congress to take an appropriation back if there has been no action on a grant. EPA guidelines for FY 03 STAG grants are currently being reviewed internally by EPA. States should get a chance to review them in June. The guidelines should be finalized by July 2003.

Since STAG grants are not going away, EPA needs to figure out how to get the SRF reviews accepted as the NEPA review. State oversight should cover the planning, design, and building phases of a project. Specific oversight requirements and reimbursement amounts should be negotiated between a state and its region. Some states may need the 3% set-aside to oversee the building phase alone. Planning and design costs are eligible even if they occur before the earmark.

Discussion

State work group members shared their experience coordinating project information with congressional representatives. Every year, Montana forwards its priority list to its congressional delegation. The result has been that 90% of STAG earmarks in Montana go to the neediest systems. The work group needs to determine how to remind congressional representatives about the regulations that apply to STAG earmark recipients.

If a community does not use an earmark, the Congressional representative often amends the earmark in future appropriation bills so that the money can be shifted to a different community. Some regions have been telling states that earmarks where the intended recipient is unclear must be competed for at the local level. EPA Headquarters clarified that if an appropriation is to a county, but the congressional intent was that the earmark benefit a specific entity, the funds do not need to be competed. OGC ruled on that matter several years ago, but EPA needs to clarify the policy.

VIII. OMB Initiatives - Lisa August, OMB Examiner

As the eyes and ears of the President, OMB helps facilitate a unifying message for the executive branch. The office tries to make sure that the objectives of the President are

being met and that all agencies have a voice at the table. The President's management agenda "scorecard" includes five management issues: human capital, financial performance, competitiveness, E-government initiatives, and budget performance integration.

One of the current major initiatives of OMB is to link federal outlays to results. The mission of each program must be clearly defined as part of this analysis. In addition, OMB studies the following components of each program: strategic design, program results, and program management. The focus of OMB's PART is program results, which should tie in to the program's strategic plan. The water goal is to protect human health, to ensure that water is safe for swimming, and to protect water quality. The EPA strategic plan for the water program is in draft form and is currently being reviewed.

The PART review of block grant programs does not focus on the number of facilities, but rather on the actual health and environmental outcomes. In order to get a "yes" on this review, a program must have evidence and measured results. The most challenging task for the SRF programs is gathering data that demonstrate public health improvement. It is not enough to have water quality data on a river because that does not tell OMB whether it meets its designated uses and improves public health. The White House needs data on results so that it can make good budget decisions. OMB is interested in answering questions like whether SRF money is spurring leveraging, displacing private funding, or subsidizing communities unwilling to raise rates. Anecdotal stories are not enough—programs need to push the envelope to collect the evidence that they are meeting their goals. The challenge is greater for the CWSRF in terms of measuring environmental results. It may be necessary to take a modeling approach to measuring benefits.

The ultimate federal goal is to determine how to maximize the public health and environmental benefits of limited federal investment dollars. Programs that produce the most positive outcomes will get more attention. Most programs reviewed last year received a "results not demonstrated" grade. EPA's strategic goals must be the focus of the Agency's programs. The challenge for EPA and for states is to prove that the SRF resources are producing results. It is made trickier by the fact that EPA is dependent on states for both implementing the program and measuring the results.

Other federal funding programs have been reviewed by OMB. Last year, RUS had a higher score than the DWSRF program, but Lisa August acknowledged that EPA had been held to the highest standard. OMB is working diligently this year to improve review consistency across agencies. The ultimate goal is to answer the question—why should federal money go to the SRF rather than to other federal programs. Results of the PART evaluation may be used to develop funding recommendations in the President's budget, identify possible legislative changes, and identify recommended program management changes.

Discussion

Work group members were pessimistic about the ability of states to go back and determine which SRF dollars were responsible for which improvements. State members claimed that the most important contribution of the SRF programs is getting them to meet federal standards; the question of what public health impact these standards produce is a question for a different program. Another problem is that the SRF programs are often designed to prevent problems before they occur, which is difficult to measure.

State resources are already stretched thin; the main mission of state programs is not to collect data to prove results. In addition, there is nothing states can do now about the lack of historical data. Producing results is also difficult because monitoring is usually the first effort cut when state budgets get tight. States also noted the lack of OMB attention to STAG earmarks which are competing with SRF programs.

IX. State Questions for Discussion

Status of CWSRF Fee Policy - Greg Swartz, Arizona

Mr. Swartz formally asked EPA to reconsider its policy on fees, which makes fees that are included in the capitalization grant subject to the 4% administrative cap. He believes the policy is not necessary under the current statutory language and inconsistent with current accounting principles. He believes that the Government Accounting Standards Board's new statements make it clear that closing fees are income, which means they should not be capped by EPA. He stated that the focus should not be on how these fees are spent, but on the source of these fees. At a minimum, EPA should submit the policy to a third party for review. EPA committed to read Mr. Swartz's formal request and to consider the matter.

Discussion

Kit Farber, EPA Headquarters, stated that the current policy had been developed with a subgroup of state and EPA representatives and is in the signature chain to be published in the *Federal Register*. Several state work group members supported Greg's position and expressed hope that EPA would exercise its latitude for interpretation. One state pointed out that leveraged states should not be subject to the 4% cap.

What are the possibilities for increasing flexibility and removing time delay roadblocks in order to fund emergency projects?

EPA is often asked this question after a natural disaster. EPA has always encouraged states to put emergency bypass procedures into their DWSRF Intended Use Plans (IUPs). However, even in response to an emergency, there are federal requirements that cannot be avoided, like environmental reviews. States may be able to use email notification to put an emergency project at the top of the list. Still, the SRFs may not be the best mechanisms for emergency projects. There are other federal emergency response

programs that are better equipped when disaster strikes. States should encourage communities to use these other federal programs and then refinance projects through the DWSRF (if necessary). This gives the state the time to put the project on the priority list and in its IUP.

Discussion

Minnesota encourages communities to get short-term financing if Department of Homeland Security (formerly FEMA) resources are not available. The state then works with these communities to refinance their debt through the DWSRF. Utah has realized that environmental reviews do not need to be stumbling blocks for emergency projects.

What are the pros and cons of leveraging?

Leveraging allows states to finance more projects for more recipients at a faster pace. States that have more needs than can currently be covered with loans may want to consider leveraging. Leveraging increases the flexibility for states in how they fund projects on their priority lists. The drawbacks to leveraging are the additional cost of selling bonds and the higher interest rate charge to loan recipients. States do have tools available that can allow them to keep the loan interest rates low. For Massachusetts, which has a leveraging ratio of 3:1, the cost has been \$8,000 per \$1,000,000 to keep the interest rate at 2%. In addition, leveraged SRFs are more complex, which means that states need more sophisticated advisors and managers.

Provide an overview of Disadvantaged Business Enterprise (DBE) program provisions and a status of the rule.

The proposed DBE provisions will replace the MBE/WBE program. The new provisions will apply to entities, including small businesses, that are economically disadvantaged. Entities are no longer allowed to self-certify and must be certified by the Small Business Administration. There are also new provisions for submission of the fair share goals. Recipients can use or take reasonable race- or gender-conscious actions to meet the goals. Any entity receiving less than \$250,000 would be exempt from negotiating fair share goals, but not from the six good faith efforts or reporting requirements. Loan recipients must also maintain a bidders list. The proposed rule has cleared OMB, but has not been published yet. The goals negotiated in 2002 are good for three years. EPA urged states to comment on the rule and discuss specific state impacts, both on the costs to states and the impacts on borrowers.

What are state experiences with meeting the 15% small system provision in the DWSRF?

Several state members mentioned that the 15% small system requirement has been easy to meet because most of their communities and systems are small systems. Some states have had systems funded off their priority list by RUS. Other states have had success coordinating with RUS to figure out which funding source best matches the needs of each system and which should be funded jointly.

What are state experiences in utilizing the set-asides?

Massachusetts has had tremendous success with capacity development because it has been able to use set-asides to hire staff. The grants for wellhead protection have been moving slowly. Florida has had success contracting with the Rural Water Association to provide technical assistance. Minnesota has taken about 20% of its capitalization grant in the form of set-asides and has reported no problems in spending the funds.

X. Security Measures and the SRFs - Cayce Parrish

Before September 11, 2001, EPA had the lead authority on water infrastructure protection. The vast majority of water systems in the country are not subject to the vulnerability assessment (VA) or the emergency response plan (ERP) requirements. Experts have determined that the biggest concern is biological or radiological contamination, especially if it occurs post-treatment. Disruption of pressured water, which can be caused by conventional explosives, cyberattacks, and interdependent services (e.g., electricity), are additional vulnerabilities.

EPA's Water Protection Task Force created a VA methodology and a self-assessment tool for small systems. It granted \$51 million to the nation's largest 450 systems. The deadlines for these systems to complete their VAs was March 31, 2003—all but six utilities met this deadline. EPA has decided that the best way to help small and medium systems is to provide \$26 million in training grants to states. In addition, EPA developed a "Train-the-Trainer" workshop for small and medium systems. The Agency is also currently developing VA training workshops for all systems that serve between 50,000 and 100,000 people.

EPA has partnered with the Department of Defense and the FBI to determine which contaminants pose the greatest public health risk to the country. EPA is developing a contaminant database that will have different levels of access for different parties. EPA is also developing a response protocol to help systems know how to respond to possible instances of intentional contamination. The water ISAC, which was mandated by presidential directive, is in place, though access issues are still being ironed out.

EPA has developed the baseline threat document, which was difficult because of the need to limit access. EPA has provided copies of the document only to those that the statute required to receive a copy. EPA is writing a guidance for systems that do not have to complete a VA. EPA developed an information protection protocol for systems' VAs. EPA has incorporated protection critical infrastructure into its strategic plan. The next step for EPA is to work with systems to help them make the security enhancements that were identified in their VAs. EPA's guidance on ERPs should be released this summer. EPA's new focus is on how to provide security assistance to small and medium systems.

Discussion

One challenge for SRF programs is how to finance security enhancements while still satisfying the public involvement requirements. The funding of VAs is not problematic because the results of the study do not need to be made available to the public. If a system seeks SRF funds to create system redundancy, it could just seek funding for the system component and not disclose that the need relates to security. Still, state work group members asked for guidance on how to handle right-to-know laws, like if a member of the public asked to see a utility's invoices. States have already received many requests from systems, particularly large systems, for funding assistance for security improvements. Georgia, Florida, and New Jersey have changed their priority lists to take security needs into account.

XI. Funding Projects in a Watershed Context - Stephanie VonFeck and Kimberley Roy

The watershed approach to improving water quality has been discussed over the last ten years. Tracy Mehan, AA for Water has affirmed that EPA will be focusing on examining watersheds holistically—the issues, the threats, the contaminants, and the solutions. One of goals is to use watershed plans to guide the investment of SRF resources. In addition, the hope is to integrate the tools of the SDWA and CWA to achieve a greater level of water quality protection. The SRF programs can be key players in the integration of water quality and drinking water programs.

The watershed approach holds several implications for the CWSRF. EPA hopes to continue to accelerate integrated planning—using water quality information to make planning and funding decisions. EPA has reaffirmed its goal to annually fund at least \$200 million in NPS projects through the CWSRF. NPS funding has been growing steadily, reaching \$242 million in 2002. To date, approximately 5% of CWSRF funding and 21% of CWSRF loans have gone to NPS projects. Thirty states have voluntarily begun funding NPS projects. Nineteen states have changed their priority systems to be based on integrated planning.

One question that EPA and states have been wrestling with is whether Concentrated Animal Feeding Operations (CAFOs) should be considered point source or NPS projects. States can fund a point source solution to a NPS problem. CAFOs are point source projects and are not eligible for CWSRF assistance unless they are publicly-owned or part of a national estuary plan. The classification of medium-sized facilities is determined by each state. Animal feeding operations that have a water body running through them or that discharge directly to surface water must be considered CAFOs. West Virginia, Arkansas, and Maine have funded animal feeding operation projects; all of them have focused on small facilities and have not yet had any problems.

There are a number of DWSRF set-asides that can be used to fund source water protection (SWP) efforts. Every state took the FY 97 source water assessment and

delineation set-aside. Eleven states reserved set-aside funds for land acquisition and conservation easements, but many states have found that systems do not want to borrow money to acquire land. Overall, spending on SWP has increased over time. As states and systems complete the source water assessments, EPA expects to see an increase in funding implementation of protection efforts. Some states have used their set-asides to hire state staff to assist systems at the local level. In addition, the CWSRF is an important assistance tool for SWP efforts. EPA has no preference whether SWP projects are funded through the DWSRF or CWSRF.

States are increasingly using partnerships with organizations like the Nature Conservancy to reach out to systems. States can encourage partners to be co-signatories on SWP loans and repay the loans so that the systems will be more inclined to negotiate land acquisition/conservation easements. States such as Maine have already had some success in brokering these types of arrangements. EPA has developed a fact sheet on how SWP loans can be used for protection measures. There are over 400 people registered for the SWP conference that will be held in June in Washington, DC. All conference participants are interested in hearing about opportunities to fund source water implementation efforts. EPA is developing a land acquisition toolbox, which will be a user-friendly document that will address issues such as: priority setting, the valuation process, how long to encumber land, legal issues, stewardship, and marketing.

XII. Recap and Planning for the Next Meeting

The next meeting will be held in Boston on November 12th and 13th (after the CIFA meeting).

Attachment 1

List of Attendees

Work Group Members (and Alternates)

George Ames	EPA Headquarters	Walt Baker	UT DEQ
Veronica Blette	EPA Headquarters	Tim Banks	FL DEP
Chuck Job	EPA Headquarters	Eric Blatt	VT Water Supply Division
Sheila Platt	EPA Headquarters	Bobby Blowe	NC Division of Water Quality
Ralph Caruso	EPA Region I	Julie Cunningham	OK Water Resources Board
Alicia Suarez	EPA Region II	Jeff Freeman	MN Public Facilities Authority
Don Niehus	EPA Region III	Tom Griggs	LA DEQ
Sheryl Parsons	EPA Region IV	Chip Heckathorn	MI DEQ
Andrew Lausted	EPA Region V	Greg Mason	GA Environmental Facilities Authority
Russ Bowen	EPA Region VI	Joe McNealy	MA DEP
Nancy Healy	EPA Region VII	Anna Miller	MT Department of Natural Resources & Conservation
		Shara Stelling	WA Department of Ecology
		Dave Waldo	KS Department of Health and Environment
		Annette Witt	KS Department of Administration
		Bev Reinhold	PENNVEST

Other Attendees

Sheila Frace	EPA Headquarters	Rosalie Brodersen	WV DEP
Jordan Dorfman	EPA Headquarters	Nikki Cleaveland	Northbridge
Kit Farber	EPA Headquarters	Rudd Coffey	The Cadmus Group
Tim Gonzales	EPA Headquarters	Ron Hill	AR Soil & Water Conservation Commission
Vinh Nguyen	EPA Headquarters	Mark Kellett	Northbridge
Kimberley Roy	EPA Headquarters	Ian Kline	The Cadmus Group
Cleora Scott	EPA Headquarters	Nancy Parrillo	MA DEP
Holly Stallworth	EPA Headquarters	Ramona Rael	NM Environment Department
Stephanie VonFeck	EPA Headquarters	Kim Treadway	Northbridge
Cliff Yee	EPA Headquarters	Gary Yamamoto	CA Department of Health Services

Attachment 2

State Questions and Answers

A. SRF Reauthorization Bills

1. Allotment Formula. We question the wisdom of an allotment formula based solely on “needs.” The “pace” of the fund should also be considered. *This item is a legislative issue. Please contact your Congressman if you would like this to be considered as part of the reauthorization process.*
2. We should resist added CWSRF restrictions and requirements to make the CW program look more like the DW program. This is the wrong direction to be headed. *This item is a legislative issue. Please contact your Congressman if you would like this to be considered as part of the reauthorization process.*
3. Davis-Bacon provisions present problems and unnecessarily add costs to projects and reduce the competitiveness of the SRF. *This item is a legislative issue. Please contact your Congressman if you would like this to be considered as part of the reauthorization process.*
4. Eight quarters rule - would EPA consider revising its regulations to eliminate this requirement? *This requirement is in statute for CWSRF and in regulations for DWSRF. This requirement is necessary to ensure the timely use of funds.*

B. Programmatic

1. Extend repayment period from 20 years to at least 30 years in the CWSRF (or to the useful life of the project). Because of the current low interest rates, leveraged states are finding it difficult to be competitive with the bond market. *This item will be addressed during the discussion on the pros and cons of leveraging.*
2. The 15% small community reserve requirement for states that leverage (DWSRF) is very difficult to meet. Is an adjustment possible? *This item is included as a State question for discussion at the meeting.*
3. Is the work accomplished through DWSRF set-a-sides worthwhile or would those funds be better utilized for construction projects? Do most states utilize set-asides? *This item is included as a State question for discussion at the meeting.*
4. Can greater flexibility be provided to construct both water distribution and sewer mains at the same time to avoid digging up the street twice? *There are no requirements at the Federal level for either SRF program that would prohibit a State from doing this.*

5. EPA should review the applicability of the IUP and Project Priority List requirements for loan guarantees and not impose these requirements on them. *This item is a legislative issue. Please contact your Congressman if you would like this to be considered as part of the reauthorization process.*
6. There is some confusion on how much of a connection with “water” there must be in order for a Brownfield project to qualify for financing. It is difficult to determine how much of the remediation can be financed. *The CWSRF can pay for the water quality portions of projects, including portions of Brownfield revitalization projects. The Brownfields fact sheet EPA-832-F-01-007 establishes the following eligible projects:*
 - Phase I, II, and III site assessments
 - Excavation and disposal of underground storage tanks
 - Excavation, removal, and disposal of contaminated oil or sediments
 - Remediation of stormwater runoff
 - Monitoring of groundwater or surface water for brownfield contaminants*EPA has also said that remediating groundwater contamination from leaking underground storage tanks is also eligible. Clearly, the activities listed above are all undertaken to protect water quality. In contrast, activities such as the destruction or refurbishing of buildings or building new structures are not water quality related and thus ineligible for CWSRF funding.*
7. Discuss efforts to move toward an electronic (paperless) business platform and what issues EPA may see as important to them in our doing so. Of particular interest is how we handle electronic signatures and whether EPA may have some guidance on what their security requirements might be. *Under the Integrated Grants Management System (IGMS) grant transactions can be electronically processed using the internet and LOTUS notes. Grant transactions created in and transmitted through LOTUS notes can be signed electronically. Grant transactions created and transmitted through the internet still require a written signature on the last page which can be signed and faxed to EPA. The EPA policy for accepting LOTUS notes electronic signatures on grant transactions can be found at <http://intranet.epa.gov/ocfo/policies/policy/pa02-02.pdf>.*
8. Provide an update on the latest status of new trigger thresholds for employing MBE/WBE requirements. *This item is included as a State question for discussion at the meeting.*
9. Revise arbitrage requirements on tax exempt bonds to recognize the reality of construction projects. Eliminate intermediate milestones and simply require that projects be completed within 2 years or arbitrage must be paid. *This item is a legislative issue. Please contact your Congressman if you would like this to be considered as part of the reauthorization process.*
10. What are the possibilities for increasing flexibility and removing time delay roadblocks in order to provide funding to emergency projects? *This item is included as a State*

question for discussion at the meeting.

C. Disadvantaged Communities

1. EPA should consider “pockets” (portions) of a community to be classified as disadvantaged, rather than continuing to require the entire service area to be so classified. *This item is a legislative issue. H.R. 1560, introduced April 2, 2003, includes a provision that would allow additional subsidization, such as principal forgiveness or negative interest loans, to be provided to municipalities that meet the State’s affordability criteria, or to a municipality that does not meet the State’s affordability criteria, if the municipality seeks the additional subsidization to benefit individual ratepayers who will experience a significant hardship from the increase in rates due to the project, and the additional subsidization is directed through a user charge rate system. Additional subsidization would be limited to 30% of the capitalization grant. S. 1961, introduced last year, included a provision that would have allowed DWSRF assistance to be provided to disadvantaged users who do not reside in a disadvantaged community. Loans provided under this authority were limited to 15% of the State’s capitalization grant, and were required to be directed through the user charge rate system to disadvantaged users.*
2. What’s happening with the Small Water System Operator’s Certification Expense Reimbursement Grant (ERG) program? *To date, EPA has awarded grants to 35 states and one territory (CNMI), totaling \$74 million. Several other states are in the process of receiving ERG funds. The types of activities the ERG program is funding include: operator fees; operator training course fees; development of new operator training courses; third party contractor support for delivering operator training courses; per diem reimbursement for unsalaried operators; mileage for travel; and grant program administration. Innovative approaches to train and certify small system operators include: contractor services for pre-exam training for operators who need additional assistance; onsite training for operators in remote locations; and development of capacity development-related training courses.*
3. Is there a national priority for establishing principal forgiveness loans as a standard part of state programs? *No, there is no national priority for States to provide principal forgiveness. It is up to the State to determine if it would like to establish a disadvantaged assistance program that offers principal forgiveness loans.*
4. Has EPA done any analyses to determine how many very-low (to 0%) interest loans states can award before it starts to affect fund perpetuity? Is there a standard method for calculating this threshold? *There is no standard method for calculating this threshold. The value would be dependent on many factors, including the interest rates charged on other types of loans, the amount of principal forgiveness offered, the amount of set-asides reserved, and the return on earnings on funds waiting to be expended. EPA has made its Financial Planning Model available to states to allow them to perform*

analyses that are tailored to their unique situation using historical data reported to NIMS.

5. Is there currently any movement in modifying the CWSRF program to allow for disadvantaged community principal forgiveness loans? *This item is a legislative issue. S. 1961 included a provision that would have allowed States to provide additional subsidization (principal forgiveness), up to 30% of the capitalization grant, to: (1) treatment works for developing technical, managerial, and financial capacity; (2) to a disadvantaged community or to a community or entity that the State expects to experience significant financial difficulties and unaffordable rate increases in order to meet the requirements of the CWA. (Also, see question C.1.)*

D. Needs Survey

1. Provide a 2003 Drinking Water Needs Survey update. *This item is included as an update topic at the meeting.*
2. Where in the Clean Water Needs Survey is the Non-Point Source documentation of needs identified? *This item is included as an update topic at the meeting.*

E. Land

1. Provide guidance on funding land acquisition under CWSRF for source water protection, water quality, and 320 estuary plans. *Projects that address source water protection are eligible for CWSRF nonpoint source loans under the authority to implement 319 (nonpoint source) management plans. EPA is developing a guide to land conservation by the CWSRF and the DWSRF that will address the main issues associated with land conservation. If you have specific issues you think should be included, please contact Stephanie vonFeck at vonfeck.stephanie@epa.gov or Kim Roy at roy.kimberley@epa.gov.*
2. Remove the restriction for “willing seller” from the DWSRF program. Few projects involving land purchase move ahead with a willing seller unless a premium is paid for the land purchase. *The provision that land must be acquired from a willing seller is a statutory requirement and would require a legislative change to be removed.*
3. Clarify the policy of only allowing SRF funds to purchase land that is “integral for treatment.” This policy seems inconsistent with EPA allowing STAGs to be used without this restriction. *The policies are inconsistent due to the fact that STAG grants are not included in the Clean Water Act but, because they are grants administered by EPA, they are governed by the general grant rules set forth in 40 CFR Part 31. The SRF capitalization grants are also governed by Part 31 but the implementation of the program is governed by 40 CFR Part 35. 40 CFR Part 31 allows for the purchase of land and 40 CFR Part 35 only allows for the purchase of land integral for treatment.*

4. How is the eligibility of the purchase of land for NPS projects (i.e., environmental easements, riparian habitat, etc.) determined? *The purchase of fee simple title or easements on land that are identified and managed to protect water quality and are consistent with 319 nonpoint source management plans are eligible for CWSRF funding. Techniques CWSRF programs, DWSRF programs and land trusts use to identify and evaluate property will be highlighted in a new SRF guide to land conservation. Often states will place higher priority on land directly adjacent to water bodies and areas where soils allow for rapid aquifer recharge in an effort to buffer ground and surface water from pollutants.*

F. STAGs

1. Discuss how some states seem to be able to influence which communities receive or do not receive STAGs. *This item will be addressed at the meeting as part of the session on coordination on STAG earmark projects.*
2. Is there any way to operate STAGs under the same rules as the SRF program? *This item will be addressed at the meeting as part of the session on coordination on STAG earmark projects.*
3. Is EPA responsible for the environmental reviews for STAG projects across all EPA regions? Under what criteria may a state be delegated environmental reviews using EPA approved, State Environmental Review Procedures (SERP)? *This item will be addressed at the meeting as part of the session on coordination on STAG earmark projects.*

G. Fees

1. Is there a simple and final policy on the use of fees? A draft guidance document is all that is available and it is way too complicated. Can the policy be revisited, simplified and finalized? *This item is included as an update topic at the meeting.*
2. Concerns remain as to the use restrictions of program income versus non-program income. We request EPA clarify this issue.

Fees from loans made with funds directly made available by the capitalization grant are designated as program income. The use of program income collected during the grant period are governed by general grant regulations at 40 CFR section 31.25. The use of these fees is limited to eligible purposes of CWA title VI and state match. The use of program income collected after the grant period are governed by EPA's authority to limit fee use as provided under 40 CFR section 31.25(h). The use of these fees is limited to eligible purposes of CWA title VI, state match, other water quality related purposes, and the combined financial administration of the CWSRF and DWSRF Funds where the programs are administered by the same state agency. Fees from loans made with non-federal funds are not designated as program income. The use of these fees is governed

by EPA's authority to specify program requirements as provided under CWA section 602(a). The use of these fees is limited to eligible purposes of CWA title VI, state match, other water quality related purposes, and the combined financial administration of the CWSRF and DWSRF Funds where the programs are administered by the same state agency (i.e., the same uses as for program income collected after the grant period).

3. Can non-program fees be sheltered within the SRF to protect them from the state budgeting process, while still allowing them to retain their "state fund" identity?

Once deposited into the CWSRF, fees are subject to the CWA's provisions covering the use of CWSRF funds. Permissible uses of the CWSRF are provided under section 603(d) and eligible purposes of fund activities are provided under section 601(a). Once deposited into the CWSRF, fees are subject to the 4 percent cap on administration costs, may not be used for water quality purposes other than those specifically allowable under title VI, and may not be used for state match unless so designated prior to being deposited into the fund.

4. Obtain an accountant's opinion on EPA's position that closing fees are subject to the 4% administrative cap. Doing so would resolve a long-standing feud between the states and EPA. The accountant could be EPA OIG staff or a third party. *This item will be addressed at the meeting.*

H. Fund Transfers

1. Explore the possibility of "loaning" funds between the CWSRF and DWSRF. Payback could be through dedicated repayments or through a future cap grant. Make this a more informal process than the current "transfer" provisions so that the governor's approval is not required. Perhaps a drinking water project could be funded through the CWSRF with all repayments from that project going to the CWSRF. *This item is a legislative issue. The types of eligible recipients and assistance that states can provide are in the SDWA. Please contact your Congressman if you would like this to be considered as part of the reauthorization process.*
2. Discuss the ability to intermingle administrative funds between the CWSRF and DWSRF programs when both programs are being administered together. *The SDWA allows States to combine financial administration of the DWSRF program and CWSRF program Funds where the programs are administered by the same State agency as long as funds are accounted for separately.*

I. NPS Projects

1. Provide an overview of the extent to which the CWSRF is being used to fund NPS and estuary protection projects versus the more traditional kinds of projects. *This item will be addressed at the meeting as part of the session on funding projects in a watershed*

context.

2. What percent of CWSRF monies are being used for 319 Projects? *This item will be addressed at the meeting as part of the session on funding projects in a watershed context.*
3. How effective are the NPS programs in other states? *This item will be addressed at the meeting as part of the session on funding projects in a watershed context.*
4. What alternatives exist or may be developed to make confined animal feeding operation (CAFO) projects eligible for CWSRF funding? *This item will be addressed at the meeting as part of the session on funding projects in a watershed context.*

J. Audits

1. Provide a status report of the various OIG, GAO, etc., evaluations. *This item is included as an update topic at the meeting.*
2. Will EPA OIG re-audit states that have already implemented independent annual audits of their program? If so, what criteria will be used to select those states? What incentive is there for states to go to the added expense of annual independent audits if OIG will re-audit every 2-3 years anyway? *Every 2-3 years, the EPA OIG will conduct audits of SRF programs that do not have independent annual audits. If a State fails to conduct an independent audit or if the EPA OIG believes that a State's independent audit is unsatisfactory, the EPA OIG may arrange for an EPA audit.*

K. Leveraging

1. Provide information/guidance for states that are thinking about leveraging or considering transferring funds between the CWSRF and DWSRF. *Chapter 3 of the "State Revolving Fund: Training Manual," released by the Council of Infrastructure Financing Authorities (CIFA) and EPA in September 2002 provides information for states that are thinking about leveraging. EPA released a final policy entitled "Transfer and Cross-collateralization of Clean Water State Revolving Funds and Drinking Water State Revolving Funds" in October 2000 which provides guidance on transferring funds.*
2. Provide the pros and cons of leveraging. *This item is included as a State question for discussion at the meeting.*

L. Communication

1. Explore a central SRF contact list that can be maintained and accessed with the internet. *The idea of a listserv is included as a discussion item at the meeting.*

2. With the delay of the DBE regulations and turnover among EPA regional staff, administering the MBE/WBE program has become confusing. Please review current requirements and basic guidelines and provide guidance on how utilization percentages should be calculated for reporting purposes, how new availability studies should be used to modify fair share percentages, etc. *This item is included as a State question for discussion at the meeting.*

M. Eligibility

1. EPA should allow broader SRF eligibility for the costs of relocating water lines, when such relocation is necessary. *There are no requirements at the Federal level for either SRF program that would prohibit a State from paying for the costs of relocating water lines if a State determined that such relocation is necessary.*
2. What are the eligibility criteria for water conservation projects (quantity) where conservation is a high priority and the identified projects will have beneficial impacts? *EPA is currently working on a fact sheet that will clarify the eligibility criteria for water conservation projects under the CWSRF and DWSRF programs.*
3. Is there currently any movement in modifying the eligibility for dam construction as part of drinking water source development? *There is no movement to modify the eligibility of dam construction under the DWSRF program. The construction and rehabilitation of dams is an ineligible activity under the DWSRF Final Rule.*

Attachment 3

Georgia Program Benefit Metrics & Indicators by Category

Category #1

HUMAN HEALTH

- Percentage of impaired water streams/river bodies brought into compliance with water quality standards for designated uses (i.e. fishing, swimming, or recreational criteria) using GEFA RLFs.
- Gallons of potable water created, clean, or developed to drinking water standards using GEFA RLFs.
- Number of septic tanks and/or contaminated wells replaced with GEFA RLFs.

Category #2

ENVIRONMENTAL

- Number of and/or percentage of impaired streams (303d) or stream segments improved and/or restored as a result of GEFA RLF projects.
- Drinking water projects or wastewater treatment improvements to meet conditions under consent or administrative orders to comply with environmental standards using GEFA RLFs.
- Best Management Practices installed to deal with non-point source problems using GEFA RLFs.

Category #3

ECONOMIC DEVELOPMENT

- Capacity increased in water and/or wastewater facilities to enable economic development.
- Commercial and/or industrial expansion (i.e. jobs created, tax base increased, etc,) occurring in community related to the use of GEFA RLFs.

Category #4

FINANCIAL

- Cost savings to borrowers using GEFA RLF as compared to private markets.
- State vs. federal funds invested and leveraged.
- Percentage of the state's annualized municipal water and sewer infrastructure financing needs as reported by the current Congressional Clean Water and Drinking Water Needs survey.